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In the Supreme Court of the United States

OCTOBER TERM, 1992

CHARTER FEDERAL SAVINGS BANK, PETITIONER

v.

DIRECTOR, OFFICE OF THRIFT SUPERVISION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether federal regulators promised a savings institution that it could use supervisory goodwill, an intangible asset, to satisfy regulatory capital standards without regard to subsequent statutory changes in the governing regulatory framework.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-21a) is reported at 976 F.2d 203. The opinion of the district court (Pet. App. 24a-59a) is reported at 773 F. Supp. 809.

JURISDICTION

The judgment of the court of appeals was entered on September 25, 1992. A petition for rehearing was denied on October 27, 1992. See Pet. App. 22a. The petition for a writ of certiorari was filed on January 4, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner Charter Federal Savings Bank was created as the result of a series of acquisitions approved by the Federal Home Loan Bank Board (Bank Board) in the 1980s. In 1981, petitioner's predecessor, First Federal Savings and Loan of Bristol, Virginia, agreed to merge with two other troubled Virginia savings institutions, First Federal Savings and Loan of New River Valley, and Peoples Federal Savings and Loan of Roanoke. Pet. App. 5a; see Pet. 3 n.1. That merger was approved in January 1982 by the Bank Board, which permitted the resulting institution (now renamed Charter) to treat the negative net worth of the acquired thrifts as an intangible asset, called "supervisory goodwill," for purposes of satisfying regulatory capital requirements. Pet. App. 5a-6a.[1] Petitioner informed its regulators that it planned to amortize over 40 years (later reduced to 25 years) the supervisory goodwill resulting from the merger with New River and Peoples. *Id.* at 6a & n.3.

In 1985, petitioner agreed to acquire New Federal Savings and Loan, an institution created from five failed thrifts in Knoxville, Tennessee. Pet. App. 6a-7a & n.4. As in 1982, the Bank Board permitted petitioner to treat the difference between the value of the thrifts and the price it paid to purchase them (some $15 million) as supervisory goodwill, which

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[1] Permitting acquiring thrifts to treat supervisory goodwill as an asset to be amortized over an extended period enabled the institutions to absorb the negative tangible net worth of the institutions they acquired without running immediately afoul of regulatory capital standards. Pet. App. 4a.

petitioner is amortizing over a 15-year period. *Id.* at 7a. Later the same year, petitioner acquired another failed Knoxville thrift, Magnolia Federal Savings and Loan. *Ibid.* Petitioner again treated the supervisory goodwill thereby generated (amounting to only $24,000) as a regulatory asset to be amortized over 15 years. *Ibid.*

2. In 1989, Congress enacted the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA), Pub. L. No. 101-73, 103 Stat. 183. As part of a wide-ranging reform of federal regulation of the nation's savings and loans, FIRREA abolished the Bank Board and replaced it with the Office of Thrift Supervision (OTS). In addition, amid substantial criticisms of the "capital gimmicks" that had led to the savings and loan crisis, H.R. Rep. No. 54, 101st Cong., 1st Sess. Pt. 1, at 310 (1989), Congress placed severe restrictions on the use of supervisory goodwill as an asset to satisfy regulatory capital standards. Thrifts were required, *inter alia*, to phase out over five years the use of supervisory goodwill to satisfy the statute's "core capital" standards, 12 U.S.C. 1464(t)(3)(A),[2] and to amortize the supervisory goodwill included in core capital annually at a rate that would lead to full amortization in a maximum of 20 years, 12 U.S.C. 1464(t)(9)(B). Thrifts were also prohibited from using supervisory goodwill at all to

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[2] All references in this brief to provisions of Title 12 of the United States Code are to the United States Code (Supp. III 1991).

satisfy the statute's "tangible capital" standard. 12 U.S.C. 1464(t)(9)(C).[3]

With supervisory goodwill excluded, petitioner had a negative net worth of approximately $19 million. Pet. App. 8a n.6. It therefore submitted a capital plan, as required by the new statute, describing the manner in which it proposed to increase its capital to achieve compliance with regulatory standards. See 12 U.S.C. 1464(t)(6)(A)(ii)(II). OTS rejected petitioner's capital plan as inadequate and based on optimistic operating projections, and refused to grant the institution a discretionary exemption from the regulatory standards. Pet. App. 8a-9a.

3. Petitioner thereafter filed suit in federal district court against OTS and the Federal Deposit Insurance Corporation (FDIC), alleging that it had binding contracts with the government permitting it to treat supervisory goodwill as an asset for purposes of satisfying regulatory capital standards. Among other things, petitioner sought a declaration that its rights to use supervisory goodwill had been preserved by FIRREA, or in the alternative, that FIRREA

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[3] In Congress's view, goodwill was "one of the remaining poisons of the savings and loan industry" (135 Cong. Rec. 12,068 (1989) (Rep. Price)), and its use was entirely antithetical to the goal of requiring greater thrift capital. See generally *Transohio Savings Bank* v. *Director, Office of Thrift Supervision*, 967 F.2d 598, 603-604 (D.C. Cir. 1992). As Senator Bradley explained, rather than reflecting the value of a thrift's franchise, "goodwill has come to mean the difference between the liabilities and the assets of a thrift, less the capital that the acquiring interest is willing to contribute. The effect is perverse—the weaker a thrift, the more goodwill it creates. This is just wrong." 135 Cong. Rec. 18,856 (1989).

frustrated the essential purpose of its prior acquisitions, permitting those acquisitions to be rescinded. Pet. App. 9a-10a.

After dismissing the government's threshold jurisdictional objections (Pet. App. 34a-45a), the district court found that petitioner and its regulators had formed an implied contract regarding the use of supervisory goodwill, that the contract was abrogated by FIRREA, and that rescission was an appropriate remedy. The court stated that by approving petitioner's "accounting proposals," the Bank Board had made an "implicit promise" to the institution to permit it to treat supervisory goodwill as a regulatory asset, to be amortized over an extended period of time. *Id.* at 46a. The court "recognize[d] that the [Bank Board] did not promise not to alter its regulations in the future," but found that fact relevant only to determining the appropriate remedy. *Id.* at 46a-47a.

The court rejected petitioner's claim that FIRREA exempted institutions with such agreements from the operation of the supervisory goodwill restrictions, upholding as "plausible" the respondents' contrary interpretation of the statute. Pet. App. 47a-51a. However, the court stated, if respondents' application of FIRREA made performance of the contract illegal, which would occur if petitioner were placed in receivership or all new loans and investments were banned, rescission would be an "appropriate remedy." *Id.* at 51a, 54a-55a. The court therefore ordered that government enforcement actions predicated on the exclusion of supervisory goodwill that "sub-stantially burden[ed]" petitioner's operations "will rescind the contract and return the institutions to their status

quo ante for the purposes of such enforcement action." *Id.* at 60a-61a.[4]

4. The court of appeals reversed. The court first agreed that the district court had jurisdiction over petitioner's suit against OTS, but found that "the tentative nature of the FDIC's involvement" rendered petitioner's claims against that agency "not ripe." Pet. App. 12a-14a.[5]

On the merits, the court of appeals expressed serious doubts whether a contract existed at all. The court noted that "no express, written contract exists between the parties," observing that the relevant Bank Board resolutions "merely granted that agency's approval of the merger[s] and the accounting practices employed by [petitioner] in connection therewith." Pet. App. 17a. The court therefore distinguished the case before it from others involving claims to binding contracts regarding supervisory goodwill, which "involved written agreements between the complaining thrift and the [Bank Board]." *Ibid.* However, the court found it unnecessary to

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[4] The court did not define what sorts of enforcement actions would constitute a "substantial burden" on petitioner's operations, other than making clear that placing the institution in conservatorship or receivership, or banning all loans or investments, would qualify. Pet. App. 61a. The court also did not explain how the contract could be rescinded, other than stating that OTS and FDIC would have to "treat the savings associations that were merged with plaintiff in 1982 and 1985 as separate entities." *Ibid.*

[5] The court of appeals declined to decide whether the lower court's order constituted an injunction that, under the statute, the lower court would not have had jurisdiction to enter. Pet. App. 15a.

decide whether there was a contract, because it determined that the terms of any such contract did not include the commitment on which petitioner based its case. *Id.* at 18a.

The court noted that the Bank Board "never expressly waived its right to enforce further regulations governing supervisory goodwill"; instead, the Bank Board approved petitioner's use of supervisory goodwill "under its then statutory discretion to permit such accounting practices." Pet. App. 20a. But, although "the [Bank Board] assured petitioner that its use of supervisory goodwill was permissible under the then current law and that the [Bank Board] would approve such practices under such law," it had "made no explicit promise to [petitioner] of continued approval throughout the life of the amortization period," regardless of any change in statutory requirements. *Ibid.* Relying on decisions of the Eleventh and D.C. Circuits in similar supervisory goodwill cases, the court concluded that "[w]ithout a more explicit promise," it would not "enlarge the scope of guarantees given to [petitioner]." *Ibid.* (citing *Transohio Savings Bank* v. *Director, OTS*, 967 F.2d 598 (D.C. Cir. 1992); *Guaranty Financial Servs., Inc.* v. *Ryan*, 928 F.2d 994 (11th Cir. 1991)).[6]

The "highly regulated nature of the savings and loan industry," including regulatory requirements for capital adequacy, which "have been an evolving

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[6] Petitioner notes (Pet. 18 n.8) that a petition for rehearing and suggestion for rehearing en banc were filed in *Transohio*. The petition and suggestion were denied on January 5, 1993, without any judge calling for a vote. *Transohio Savings Bank* v. *Director, OTS*, No. 91-5246 (D.C. Cir.).

part of the regulatory scheme since its inception," also persuaded the court that, "absent an explicit statement to the contrary, the [Bank Board] would not have intended to promise [petitioner] continued treatment of supervisory goodwill as capital for the life of the amortization period." Pet. App. 20a. The court noted that "the [Bank Board] would have expected changes in statutory requirements, including capital requirements" and the court found it "doubtful * * * that the [Bank Board] intended to secure to [petitioner] the use of supervisory goodwill over a fifteen to twenty-five year period." *Id.* at 20a-21a. As a savings and loan, the court observed, petitioner "certainly was cognizant of the regulatory intrusions into this business." *Id.* at 21a. The court concluded that, "[i]f [petitioner] wanted to avoid the risk of regulatory change, it could have demanded more explicit assurances." *Ibid.*[7]

ARGUMENT

The court of appeals correctly determined that government regulators never promised petitioner that it could treat supervisory goodwill as a regulatory asset, irrespective of subsequent statutory reforms. That determination, which is tied to the facts of this case, does not conflict with any decision of this Court or any other court of appeals. Further review is therefore unwarranted.

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[7] Because it held that the Bank Board had not waived the right to enforce subsequent statutory changes in supervisory goodwill requirements, the court of appeals found it unnecessary to determine whether rescission would have been an appropriate remedy had the Bank Board contracted to waive its rights and then reneged on the bargain. Pet. App. 21a.

1. The court of appeals' decision is correct. As this Court has explained:

> "[S]overeign power, even when unexercised, is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms." * * * Therefore, contractual arrangements, including those to which a sovereign itself is [a] party, "remain subject to subsequent legislation" by the sovereign.

Bowen v. *Public Agencies Opposed to Social Security Entrapment*, 477 U.S. 41, 52 (1986) (quoting *Merrion* v. *Jicarilla Apache Tribe*, 455 U.S. 130, 147-148 (1982)). Thus, "one who wishes to obtain a contractual right against the sovereign that is immune from the effect of future changes in law must make sure that the contract confers such a right in unmistakable terms." *Western Fuels-Utah, Inc.* v. *Lujan*, 895 F.2d 780, 789 (D.C. Cir.), cert. denied, 111 S. Ct. 47 (1990).[8]

In light of that rule, it was entirely appropriate for the court of appeals to have refused to "enlarge the scope of guarantees given to [petitioner]." Pet. App. 20a. The court's conclusion was buttressed by a number of other factors, including the lack of any "express, written contract" between petitioner and

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[8] Accord *Transohio*, 967 F.2d at 618; *Guaranty*, 928 F.2d at 1001; *Peterson* v. *United States Department of Interior*, 899 F.2d 799, 807 (9th Cir.), cert. denied, 111 S. Ct. 567 (1990). See also *Great Lakes Higher Educ. Corp.* v. *Cavazos*, 911 F.2d 10, 16 & n.13 (7th Cir. 1990); *Education Assistance Corp.* v. *Cavazos*, 902 F.2d 617, 629 & n.20 (8th Cir.), cert. denied, 111 S. Ct. 246 (1990).

its regulators (*id.* at 17a); the absence of any "explicit promise" that petitioner would be entitled to continued approval of its regulatory accounting practices (*id.* at 20a); and the "highly regulated nature of the savings and loan industry," including the imposition of "evolving" capital requirements on industry participants (*ibid.*). Indeed, it would have been entirely unreasonable for any participant in the "highly regulated" thrift industry to have assumed that it could obtain by implication the rights that petitioner asserts it was granted here.

Although petitioner suggests that it "never would have" agreed to the 1982 and 1985 acquisitions without assurances that it would be able to treat supervisory goodwill as capital over an extended period of time (Pet. 4), the court of appeals reasonably presumed that petitioner could have "accounted for the risk of regulatory change" in deciding whether or not to acquire the failing thrifts. Pet. App. 21a. Petitioner was fully represented by counsel in the various transactions, and, had it deemed assurances concerning future statutory change indispensable, it should have demanded "more explicit assurances." *Ibid.*[9] "[I]n effect," thrifts like petitioner "wager[ed] the chance that the rules would be changed against the potential return if they were not." *Transohio*, 967 F.2d at 620 (quoting *Guaranty*, 928 F.2d at 999). Having lost its wager, petitioner cannot complain about changes that Congress found necessary to

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[9] Ironically, petitioner in fact obtained—at least in a letter from the Bank Board—just such an express assurance concerning regulatory forbearance. See Pet. App. 17a n.11. But that express assurance by its terms expired in 1990.

protect the public interest in a sound savings and loan industry.

The decision below is firmly supported by the D.C. Circuit's decision in *Transohio Savings Bank* v. *Director, OTS, supra*, and the Eleventh Circuit's decision in *Guaranty Financial Servs., Inc.* v. *Ryan, supra*, both of which rejected claims by thrifts to contracts with the federal government regarding supervisory goodwill in similar circumstances. As in this case, the *Transohio* and *Guaranty* courts refused to find that the federal government had promised to immunize a party from future changes in federal law unless such a right is expressed in "unmistakable terms." *Transohio*, 967 F.2d at 618; *Guaranty*, 928 F.2d at 1001.

Petitioner attempts to distinguish *Transohio* and *Guaranty* on the ground that they involved claims for injunctive relief, not rescission. Pet. 18. But the form of relief sought is beside the point. The issue in each case, as in the decision below, was whether the facts peculiar to the case demonstrate that the thrift obtained a contract right to the use of supervisory goodwill as regulatory capital over a specified time period, regardless of any subsequent statutory change. The question of remedy would arise only if such a contract right were found to exist. Like the courts in *Transohio* and *Guaranty*, the court of appeals in this case did not reach any remedial issue precisely because it found that no such right had been granted.

2. Petitioner asserts (Pet. 11-13) that the decision below conflicts with decisions of several district courts, as well as decisions of the Court of Federal Claims. Initially, each of the cases cited by petitioner

involves distinct transactions, and a decision that banking authorities entered into, and later breached, a contract concerning supervisory goodwill in one case would not lead to the same conclusion on the entirely different facts of another case. In any event, the Court does not ordinarily grant review to resolve a conflict between a court of appeals' decision and one or more trial court decisions. Review would be particularly inappropriate here, because three courts of appeals have reached the relevant issues, and they are all in agreement.[10]

3. This case need not be held pending the Court's decision in *Cisneros* v. *Alpine Ridge Group*, No. 92-551 (to be argued March 30, 1993). *Alpine Ridge* involves contracts between the Department of Housing and Urban Development and private housing developers. It presents questions concerning the interpretation of the contracts and the scope of any substantive due process limits on legislation that modified them.

This case is unlikely to be affected by this Court's resolution of the issues in *Alpine Ridge*. The court of appeals ruled that whatever contract could have

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[10] We note that one of the trial court decisions cited by petitioner (*Ensign Financial Corp.* v. *FDIC*, 785 F. Supp. 391 (S.D.N.Y. 1992)) was overturned on February 16, 1993, after reconsideration. The others are currently on appeal. See *Winstar Corp.* v. *United States*, No. 92-5164 (Fed. Cir.) (argued Jan. 6, 1993); *Security Federal Savings & Loan Ass'n of Albuquerque* v. *FSLIC*, 796 F. Supp. 1435 (D.N.M. 1991), appeals filed, Nos. 93-2002, 93-2015 & 93-2016 (10th Cir.); *Far West Federal Bank, S.B.* v. *Director, Office of Thrift Supervision*, 787 F. Supp. 952 (D. Or. 1992), appeals filed, Nos. 92-35597 & 92-36535 (9th Cir.).

been formed in this case did not include the crucial promise on which petitioner relies. This case, unlike *Alpine Ridge*, thus presents no question concerning the circumstances under which Congress may abrogate vested contract rights.

Nor do the contract interpretation issues in *Alpine Ridge* have any relevance to this case. In *Alpine Ridge*, the parties contest the proper interpretation of particular, express contract provisions governing the private contractors' authority to impose annual rent increases. See *Alpine Ridge Group* v. *Kemp*, 955 F.2d 1382, 1387 (9th Cir.) (contract provisions "unambiguously stated in * * * the contracts themselves"), cert. granted, 113 S. Ct. 490 (1992) (No. 92-551). In this case, petitioner's argument rests on speculation concerning the content of an alleged unwritten, non-express "contract" governing supervisory goodwill. There is no reason to believe that the interpretation of the housing subsidy contracts in *Alpine Ridge* will provide any guidance in interpreting whatever contract petitioner could claim was formed in this case. Indeed, the court of appeals in *Alpine Ridge* took care to distinguish decisions—such as the one here—which "declined to interpret contracts as containing implied provisions foreclosing the exercise of sovereign power by the government." 955 F.2d at 1386.

4. Finally, although the court of appeals did not reach these questions (Pet. App. 15a, 21a), there are two additional grounds that independently support the court of appeals' judgment.

First, the district court exceeded its jurisdiction by entering what was in effect an injunction prohibiting enforcement actions by the thrift

regulatory agencies. Specifically, the district court required that, if OTS or FDIC sought to take enforcement action against petitioner predicated on FIRREA's restrictions on the use of supervisory goodwill which would "substantially burden[]" petitioner's operations, the agencies must treat petitioner's various merged predecessors "as separate entities for the purposes of such enforcement action." Pet. App. 60a-61a. In other words, the district court directed the agencies to refrain from enforcing FIRREA's supervisory goodwill restrictions against petitioner *in its existing form*. As such, the order was precluded by 12 U.S.C. 1464(d)(2)(B), (D)—which prohibits the courts from restraining the authority of the OTS Director to appoint a conservator or receiver for a thrift—and 12 U.S.C 1818(i)(1)—which prohibits the courts from affecting by "injunction or otherwise" the issuance or enforcement of any notice of charges or enforcement order issued by either OTS or FDIC. See *First Federal Savings Bank & Trust* v. *Ryan*, 927 F.2d 1345, 1355-1356 (6th Cir.) (Section 1464(d)), cert. denied, 112 S. Ct. 187 (1991); *Board of Governors* v. *MCorp Financial, Inc.*, 112 S. Ct. 459, 463-466 (1991) (Section 1818(i)).

Second, rescission would have been an inappropriate remedy in any event under the circumstances presented by this case. As a matter of law, the defense of impossibility of performance requires, among other things, the "*unexpected* occurrence of an intervening act." *Opera Co. of Boston, Inc.* v. *Wolf Trap Foundation for Performing Arts*, 817 F.2d 1094, 1102 (4th Cir. 1987) (emphasis added). Here, however, as the court of appeals found (Pet. App. 20a-21a), changes in thrift capital standards were hardly

unexpected. There are also important practical objections to rescission and restoration of the parties to the "status quo ante." *Id.* at 61a. The mergers at issue in this case were completed in 1982 and 1985, at which time the assets of the merged institutions were commingled and petitioner was operated as a single thrift. After so long a period of time, it would be impossible for government regulators to treat the merged institutions "as separate entities." *Ibid.* Thus, even if government regulators had made a binding commitment to petitioner regarding supervisory goodwill, the district court had no power to order long-completed mergers to be rescinded.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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